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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1937

No. 21

HERMAN C. GROMAN,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

Petition for Rehearing

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Petition for Rehearing

Now comes the above named Herman C. Groman, petitioner, and presents this his petition for rehearing of the above entitled cause and in support thereof respectfully shows:

1. Certain facts vital under the law of the opinion have been misapprehended.

2. It is a necessary inference from the opinion that *Helvering* v. *Watts*, 296 U. S. 387, has been overruled *sub silentio*.

1. The opinion of the Court has sustained our contention that whether the relation of the Glidden Company to the reorganization in this case was such as to constitute it a "party" thereto must be determined by "the ordinary connotation of the term [party]." But it appears that in our effort to establish the error of the Circuit Court of Appeals on this question of law we have failed to make the facts clear, because this Court has, we think, misapprehended certain vital facts, and as a result of this adopted a view of Glidden's participation in the transaction opposed to the uncontroverted record.

The opinion states (p. 5):

> "Glidden transferred nothing to them (the Indiana shareholders)."

This is incorrect. It is agreed that Glidden issued its own prior preference stock direct to the Indiana shareholders pursuant to the reorganization contract. (R. 12; Brief of Respondent, p. 4.) Glidden also guaranteed directly to the Indiana shareholders the payment of dividends on the *Ohio* stock, and the redemption of that stock within four years; so the Indiana shareholders received from Glidden in addition to the Glidden stock a commitment of Glidden to retire the Ohio stock. (R. 12.)

The opinion further states (p. 5):

> "The exchange was between Indiana's shareholders and Ohio. * * * Glidden contracted for the exchange and made it possible by subscribing and paying for Ohio's common stock in cash and prior preference stock so that Ohio could consummate the exchange. * * *"

This is incorrect; and this same error occurs in the opinion of the Circuit Court of Appeals. (R. 46.) There is no support in the record for the view that the common stock of Ohio was paid for in part by the prior preference stock of Glidden, or that Ohio ever owned any

Glidden stock. On the contrary, the fact that Glidden issued its prior preference stock direct to the Indiana shareholders indicates that this stock was not issued to Ohio. And the corollary fact that Glidden acquired the Ohio common stock for *cash* is affirmatively shown by the record. (R. 12, 21.)

In the light of these facts the comparison of Glidden's position in the transaction to that of a broker, promoter or agent is seen at once to be inappropriate. Its participation was not subordinate, but that of a principal. It was not a catalyst, or even a reagent, but its own chemical constitution was definitely altered in a reaction in which it was an indispensable constituent. It could not be Ohio's agent, because it was Ohio's creator. It could not be the agent of Indiana's stockholders, because it contracted with them at arm's length. It could not be a broker, because its contract was entirely for its own account; it had no principal to represent. A promoter is one who procures the investment of capital by others; Glidden's own capital was the basis of the reorganization, and there was no other new contribution. In so far as participation as a principal party in interest is the test of "partyship," the true facts make it clear that Glidden satisfied this requirement more fully than Ohio did; and participation as a principal is the basic idea in "the ordinary connotation of the term [party]."

2. The last page of the opinion says that to treat Glidden as a party here would violate the spirit of the Revenue Act because there is no sufficient continuity of interest *qua* the Glidden stock. We believe that the effect of this holding under the facts as they actually exist is to overrule the holding of this Court in *Helvering* v. *Watts*, 296 U. S. 387, although the *Watts* case is not discussed in this connection in the opinion.

In that case Watts exchanged his stock in Ferro-Alloys for bonds of that company and stock of Vanadium;

Vanadium acquired control of Ferro-Alloys, which continued to operate as a Vanadium subsidiary. This Court held that both Vanadium and Ferro-Alloys were parties to the reorganization; and both the Vanadium stock and the Ferro-Alloys bonds were received without recognition of gain. The continuity of Watts' interest in the assets of Ferro-Alloys, *qua* the Vanadium stock, was diluted by the acquisition of an interest in all Vanadium's other assets, just as in this case Groman's interest in the assets of Indiana, *qua* the Glidden stock, is diluted by his acquired interest in Glidden's other assets. And so in every case of a merger or consolidation there is of necessity such dilution by acquisition of an interest in assets other than those transferred. (See *Nelson Co.* v. *Helvering,* 296 U. S. 374; *Helvering* v. *Minnesota Tea Co,,* 296 U. S. 378; *Helvering* v. *Bashford,* No. 33, October Term, 1937, now set for reargument December 13, 1937.)

That this of itself does not destroy continuity of interest is made clear in the opinion of this Court, in *Minnesota Tea Co.* v. *Helvering,* 296 U. S. 378:

> "True it is that the relationship of the taxpayer to the assets conveyed was substantially changed, but this is not inhibited by the statute." (P. 386.)

The plain effect of the decision in the *Watts* case is to reassert this rule and hold that the retention by stockholders of an interest in the subsidiary's business, *via* stockholding in the parent corporation, is a sufficient continuity of interest in such business to satisfy the spirit of the Revenue Act.

And is this not the correct conclusion, both as to Watts and Groman? What Congress intended was to defer the ascertainment of gain or loss until the taxpayer's stake was removed from the table, enhanced or diminished. Here Groman's interest in Indiana's assets and business continues through the Glidden stock just as definitely

and substantially as through the Ohio stock; through the Glidden stock over $700,000.00 of the original stake of the Indiana stockholders remains on the table, subject to the same hazards.

If the Court in the *Watts* case had said (substituting the other names for those in the opinion here): "Was not Vanadium's stock 'other property' in the sense that its ownership represented a participation in assets in which Ferro-Alloys, and its shareholders through it, had no proprietorship," it seems to us the answer which would support the *Watts* opinion would be that whether Ferro-Alloys, or its stockholders through it, had a proprietorship in *Vanadium's* assets, is not relevant to the inquiry; the relevant question is whether the original Ferro-Alloys shareholders, through the *Vanadium* stock, retained a definite substantial proprietary interest in *Ferro-Alloys* original assets. So here we submit it is not material whether Ohio, or its shareholders *through it,* have any proprietorship in the assets of Glidden; the continuity of interest which the spirit of the law requires is the retained interest by Indiana's original stockholders, *through stock in Glidden,* in the former assets of Indiana, now held by Glidden's subsidiary.

We submit that under the true facts of this case the interest of the Indiana stockholders "continues to be definitely represented in substantial measure" *through the Glidden stock* equally as was Watts' interest through the Vanadium stock in the *Watts* case, and unless the *Watts* case is to be overruled, the opinion here should be changed. To do so neither disregards the letter nor violates the spirit of the Revenue Act as interpreted by prior decisions of this Court.

For the foregoing reasons, it is respectfully urged that this petition for rehearing be granted and that the judg-

ment of the Circuit Court of Appeals for the Seventh Circuit be, upon further consideration, reversed.

Respectfully submitted,

EGBERT ROBERTSON,
JAMES C. SPENCE,
Counsel for Petitioner.

CERTIFICATE OF COUNSEL.

We, Egbert Robertson and James C. Spence, counsel for the above named Herman C. Groman, petitioner, do hereby certify that the foregoing petition for rehearing of this cause is presented in good faith and not for delay.

EGBERT ROBERTSON,
JAMES C. SPENCE,
Counsel for Petitioner.

P 5,

SUPREME COURT OF THE UNITED STATES.

No. 21.—October Term, 1937.

Herman C. Groman, Petitioner,
vs.
Commissioner of Internal Revenue.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.

[November 8, 1937.]

Mr. Justice Roberts delivered the opinion of the Court.

This case involves the meaning and scope of the phrase "a party to a reorganization" as used in Section 112 of the Revenue Act of 1928.[1]

January 29, 1929, the petitioner, and all other shareholders of Metals Refining Company, an Indiana corporation, hereinafter designated Indiana, entered into a contract with the Glidden Company, an Ohio corporation, reciting that the shareholders of Indiana were desirous of merging and consolidating the properties of their company with Glidden and with a corporation Glidden was to organize under the laws of Ohio, which corporation we shall call Ohio. The shareholders covenanted that they would assign their shares to Ohio, which was to have a specified capital structure divided into preferred and common shares, and Glidden covenanted that it would issue and deliver, or cause to be issued and delivered to the shareholders a stated number of shares of its own prior preference stock at an agreed valuation, a stated number of shares of the preferred stock of Ohio, also at an agreed valuation, and sufficient cash to equal the appraised value of Indiana's assets as of March 1, 1929, and that, after the exchange of stock, Glidden would cause Indiana to transfer its assets to Ohio.

Glidden organized Ohio and became the owner of all its common stock but none of its preferred stock. Pursuant to the contract the shareholders of Indiana transferred their stock to Ohio and received therefor a total consideration of $1,207,016 consisting of Glidden prior preference stock valued at $533,980, shares of the

[1] Ch. 852, 45 Stat. 791, 816.

preferred stock of Ohio valued at $500,000, and $153,036 in cash. Indiana then transferred its assets to Ohio and was dissolved.

As a result of the reorganization petitioner received shares of Glidden stock, shares of Ohio stock, and $17,293 in cash. In his return for 1929 he included the $17,293 as income received but ignored the shares of Glidden and of Ohio as stock received in exchange in a reorganization. The respondent ruled that Glidden was not a party to a reorganization within the meaning of the Revenue Act, treated the transaction as a taxable exchange to the extent of the cash and shares of Glidden, and determined a deficiency of $7,420. Upon receipt of notice to this effect the petitioner appealed to the Board of Tax Appeals which reversed the Commissioner, holding that Glidden was a party to a reorganization. The Circuit Court of Appeals reversed the Board.[2] We granted the writ of certiorari because of an alleged conflict of decision.[3]

Section 112 (b) (3) of the Revenue Act of 1928 declares that "No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization." If the transaction involves the receipt of such stock or securities and "also of other property or money" then the gain, if any, is to be recognized in an amount not in excess of the sum of such money and the fair market value of such other property. [Section 112 (c) (1).]

Section 112 (i) (1) declares: "The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place of organization, however effected." Subsection (2) is: "The term

[2] 86 F. (2d) 670.

[3] See *Sage* v. *Commissioner*, 83 F. (2d) 221; *Commissioner* v. *Fifth Avenue Bank*, 84 F. (2d) 787; *Commissioner* v. *Bashford*, 87 F. (2d) 827.

'a party to a reorganization' includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation."

It is agreed that under the plain terms of the statute the cash received by the petitioner was income, and that as the stock of Ohio was obtained in part payment for that of Indiana, the exchange, to that extent, did not give rise to income to be included in the computation of petitioner's tax.

The question is whether that portion of the consideration consisting of prior preference shares of Glidden should be recognized in determining petitioner's taxable gain. The decision of this question depends upon whether Glidden's stock was that of a party to the reorganization for, if so, the statute declares gain or loss due to its receipt shall not be included in the taxpayer's computation of income for the year in which the exchange was made.

If Section 112 (i) (2) is a definition of a party to a reorganization and excludes corporations not therein described, Glidden was not a party since its relation to the transaction is not within the terms of the definition. It was not a corporation resulting from the reorganization; and it did not acquire a majority of the shares of voting stock and a majority of the shares of all other classes of stock of any other corporation in the reorganization. The Circuit Court of Appeals thought the section was intended as a definition of the term party as used in the Act and excluded all corporations not specifically described. It therefore held Glidden could not be considered a party to the reorganization.

The petitioner contends, we think correctly, that the section is not a definition but rather is intended to enlarge the connotation of the term "a party to a reorganization" to embrace corporations whose relation to the transaction would not in common usage be so denominated or as to whose status doubt might otherwise arise. This conclusion is fortified by the fact that when an exclusive definition is intended the word "means" is employed, as in the section we have quoted defining reorganization and in Section 112 (j), defining the term "control", whereas here the word used is "includes." If more were needed Section 701 (b) declares: "The terms 'includes' and 'including' when used in a definition contained in this Act shall not be deemed to exclude other things otherwise within the meaning of the term defined."

The Treasury, in its regulations, has construed the section as not embodying an exclusive definition.[4] The administrative construction of an identical section in the Revenue Acts of 1924 and 1926 has been the same.[5]

If the shareholders of A, and those of B, should agree to convey their stock to a new corporation C, in exchange for C's stock, a reorganization, as defined in Section 112 (i) (1) would be effected. But it might well be contended, were it not for Section 112 (i) (2), that the shareholders of the old corporations had not received stock in a non-taxable exchange, as specified in Section 112 (b) (3), since the new corporation C was not a party to the exchange. In the present instance, Indiana had no part in the transaction. The shareholders agreed to transfer their stock to Ohio in exchange for securities. Indiana, as such, was not a party to any agreement and took no corporate action. If the plan had contemplated the continued existence of Indiana, and part payment of its shareholders in bonds or preferred stock of that company, and part in shares of Ohio, while this would clearly have constituted a reorganization as defined by the Act, it might, with reason, be urged that, as respects the bonds or preferred stock of Indiana, the exchange was taxable since Indiana was not a party to the reorganization. Section 112 (i) (2) precludes the contention.[6]

Plainly, however, there may be corporate parties to reorganizations, within the meaning of the statute, other than those enumerated in Section 112 (i) (2). Thus if corporations A and B transfer all their assets to C, a new corporation, in exchange for all C's stock, the stock received is not a basis for calculation of gain on the exchange.[7] A and B are so evidently parties to the reorganization that we do not need Section 112 (i) (2) to inform us of the fact.

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[4] Treasury Regulations 74, promulgated under the Revenue Act of 1928, Art. 577: "The term 'a party to a reorganization' . . . includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation. This definition is not an all-inclusive one, but simply enumerates certain cases with respect to which doubt might arise."

[5] Regulations 65, Art. 1577, applicable to Section 203 (h) (2) of the Revenue Act of 1924; Regulations 69, Art. 1577, applicable to Section 203 (h) (2) of the Revenue Act of 1926.

[6] Compare *Helvering* v. *Watts*, 296 U. S. 387.

[7] Compare *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378; *G. & K. Manufacturing Co.* v. *Helvering*, 296 U. S. 389.

Again, if company A transfers all its assets to company B, a going concern, upon the agreement of B to issue to A's shareholders its stock in such amount that they will own eighty per cent of every class of B's outstanding stock; the consummation of the agreement will be a reorganization under the Act.[3] Unquestionably the gain ensuing upon the exchange of stock by A's shareholders will not be taxable since the stock received by them is that of B, a party to the reorganization, though B is not described as such in Section 112 (i) (2). We must, therefore, irrespective of Glidden's failure to qualify as a party under that section, determine whether its relation to the reorganization is that of a party within the ordinary connotation of the term.

Glidden was a party to an agreement with the shareholders of Indiana and the agreement envisaged a reorganization as defined by Section 112 (i) (1) (A) for it contemplated that Ohio should acquire all of the stock of Indiana. The agreement was fulfilled. But the crucial question is whether Glidden was a party to the reorganization thus effected. Glidden received nothing from the shareholders of Indiana. ~~Glidden transferred nothing to them.~~ The exchange was between Indiana's shareholders and Ohio. Do the facts that Glidden contracted for the exchange and made it possible by subscribing and paying for Ohio's common stock in cash ~~and prior preference stock~~, so that Ohio could consummate the exchange, render Glidden a party to the reorganization? No more so than if a banking corporation had made the agreement with Indiana's shareholders and had organized the new corporation, and, by subscription to its stock and payment therefor in money and the banking company's stock put the new company in position to complete the exchange. Not every corporate broker, promoter, or agent which enters into a written agreement effectuating a reorganization, as defined in the Revenue Act, thereby becomes a party to the reorganization. And, if it is not a party, its stock received in exchange, pursuant to the plan, is "other property" mentioned in Section 112 (c) (1) and must be reckoned in computing gain or loss to the recipient. Glidden was, in the transaction in question, no more than the efficient agent in bringing about a reorganization. It was not, in the natural meaning of the term, a party to the reorganization.

[3] Section 112, Subsections (i) (1) (B) and (j).

It is argued, however, that Ohio was the *alter ego* of Glidden; that in truth Glidden was the principal and Ohio its agent; that we should look at the realities of the situation, disregard the corporate entity of Ohio, and treat it as Glidden. But to do so would be to ignore the purpose of the reorganization sections of the statute, which, as we have said, is that where, pursuant to a plan, the interest of the stockholders of a corporation continues to be definitely represented in substantial measure in a new or different one, then to the extent, but only to the extent, of that continuity of interest, the exchange is to be treated as one not giving rise to present gain or loss.[9] If cash or "other property",—that is, property other than stock or securities of the reorganized corporations,—is received, present gain or loss must be recognized. Was not Glidden's prior preference stock "other property" in the sense that its ownership represented a participation in assets in which Ohio, and its shareholders through it, had no proprietorship? Was it not "other property" in the sense that *qua* that stock the shareholders of Indiana assumed a relation toward the conveyed assets not measured by a continued substantial interest in those assets in the ownership of Ohio, but an interest in the assets of Glidden a part of which was the common stock of Ohio? These questions we think must be answered in the affirmative. To reject the plain meaning of the term "party", and to attribute that relation to Glidden, would be not only to disregard the letter but also to violate the spirit of the Revenue Act.

We hold that Glidden was not a party to the reorganization and the receipt of its stock by Indiana's shareholders in exchange, in part, for their stock was the basis for computation of taxable gain to them in the year 1929.

The judgment is

Affirmed.

Mr. Justice BLACK took no part in the consideration or decision of this case.

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[9] *Pinellas Ice Co.* v. *Commissioner*, 287 U. S. 462, 470; *Nelson Co.* v. *Helvering*, 296 U. S. 374, 377; *Helvering* v. *Minnesota Tea Co.*, 296 U. S. 378, 385; *G. & K. Manufacturing Co.* v. *Helvering*, 296 U. S. 389, 391.